Office of Chief Counsel
Internal Revenue Service

memorandum

CC:NER:MAN:TL-N-7404-98
JDPappas

date:

to: District Director, Manhattan District
Attn. [redacted], Case Manager
Group [redacted]

from: District Counsel, New York CC:NER:MAN

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subject: [redacted]
I.R.C. §6402(b) credit elect issue

UIL Number: 6402.01-02

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This memorandum supplements our previous memorandum dated March 19, 1999 wherein you asked for assistance in determining when deficiency interest runs in the context of an election to have a refund applied to the subsequent year's estimated tax payment. The taxpayer has recently asked to revise it Underpayment of Estimated Tax by Corporations "Form 2220", thus, providing different facts, which would change our recommendation in our prior memorandum.

ISSUES:

1. Whether underpayment interest began to accrue on [redacted] ("[redacted]") deficiency in tax for

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fiscal year ending March 31, [redacted] prior to [redacted].

2. Whether the statute of limitations bars the taxpayer's subsequent claim for refund because it is not made within the time prescribed by I.R.C. § 6511.

3. Whether the taxpayer can retroactively amend its Form 2220 to change the amounts of its estimated payments.

FACTS:

On [redacted], [redacted] filed its Form 1120 (U.S. Corporation Income Tax Return) for fiscal year ending March 31, [redacted] ("Tax Year [redacted]") (extended due date [redacted]). On its Form 1120 for Tax Year [redacted], [redacted] reported an overpayment of $[redacted][1], which [redacted] elected to have credited against its liability for estimated tax for fiscal year ending March 31, [redacted] ("Tax Year [redacted]"). However, [redacted] did not designate against which installment of estimated tax the overpayment for Tax Year [redacted] was to be applied. Thus, pursuant to Rev. Rul. 84-58, 1984-1 C.B. 254, the Service should have and did credit the overpayment against [redacted]'s estimated tax for Tax Year [redacted] as of July 15, [redacted], the due date for [redacted]'s first installment of estimated tax for Tax Year [redacted]. See also, *Avon Products v. United States*, 588 F.2d 342 (2nd Cir. 1978). [redacted]'s account was credited as of July 15, [redacted], although its estimated tax payment for that quarter turned out to be [redacted]. [redacted]'s estimated tax payments for Tax Year [redacted] were as follows:

Installment	Due Date	Amount
1st	[redacted]	$[redacted]
2nd	[redacted]	$[redacted]
3rd	[redacted]	$[redacted]
4th	[redacted]	$[redacted]

Installments 2 and 3 total the credit elect amount. Installment 4 was paid from funds other than the [redacted] overpayment.

As a result of the audit of [redacted]'s Tax Year [redacted], the Service determined that there was a deficiency of $[redacted] for that year. [redacted] paid the additional assessment of tax and interest, and on March 20, [redacted], it timely filed a claim for refund with respect to a portion of the assessed interest. We

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[1] You previously told us the overpayment was $[redacted], which we used in our original advice. That figure included $[redacted] of a credit elect from Tax Year [redacted], which was previously refunded on November 22, [redacted]. This revised refund figure would not change our previous conclusions nor does it impact on our current analysis.

advised you in our prior memorandum that interest did not begin to run until December 15, [redacted] and recommended that you refund [redacted]'s overpayment of interest.

[redacted] now contends that its quarterly estimated tax payments should have been as follows:

Installment	Due Date	Amount
1st	[redacted][2]	$[redacted]
2nd		$
3rd		$
4th		$

Thus, [redacted] now contends that with the application of the overpayment and [redacted]'s payment of $[redacted], Mitsui's entire tax did not become both due and unpaid until June 15, [redacted], the due date of the subsequent year's return. [redacted] further contends that from March 15, [redacted] until June 15, [redacted], interest should only run on the portion of the deficiency that is in excess of the remaining balance of the [redacted] overpayment after application to all four quarters. Therefore, [redacted] now claims a refund of interest that had accrued since July 15, [redacted].

LAW AND ANALYSIS:

1. The Interest On [redacted]'s Deficiency Began to Accrue on March 15, [redacted].

In general, the government is entitled to interest on a deficiency in tax for the period that the tax was due and unpaid. I.R.C. § 6601(a); *Avon Products v. United States*, 588 F.2d 342 (2d Cir. 1978). If a deficiency in tax is determined after the taxpayer elected to credit a return overpayment against its estimated tax liability for the next succeeding year, interest will begin to accrue on the amount of the deficiency equal to the amount of the return overpayment as of the effective date of the credit elect. H.R. Rep. No. 98-432 (Part I), 98th Cong., 1st Sess. 190 (Oct. 21, 1983); *see also*, Rev. Rul. 88-98, 1988-2 C.B. 356. Section 413 of the Tax Reform Act of 1984 provides that overpayments of tax will be credited against the estimated income tax for the next succeeding year with full regard to Revenue Ruling 77-475, 1977-2 C.B. 476.[3] Pub. L. No. 98-369, 98 Stat. 494. Revenue Ruling 77-475 provides:

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[2] [redacted]'s subsequent claim reflects slightly different dates from the original.

[3] In 1983, the Service revoked Revenue Ruling 77-475. Rev. Rul. 83-111, 1983-2 C.B. 245. However, in response to tremendous public criticism and expected Congressional action, the Service promulgated Revenue Ruling 84-58, 1984-1 C.B. 254, which reinstated and modified Revenue Ruling 77-475 on March 30, 1984.

> [i]f an overpayment of income tax for a taxable year occurs on or before the due date of the first installment of estimated tax for the succeeding taxable year, the overpayment is available for credit against any installment of estimated tax for such succeeding taxable year and will be credited in accordance with the taxpayer's election.

1977-2 C.B. at 476 (emphasis added). Accordingly, interest on the deficiency in the prior year begins to accrue on the due date of the installment of estimated tax for the succeeding taxable year against which the overpayment was credited in accordance with the taxpayer's designation. H.R. Rep. No. 98-432 (Part I), 98th Cong., 1st Sess. 190 (Oct. 21, 1983); *see also* Rev. Rul. 88-98, 1988-2 C.B. 356. However, the deficiency only becomes both due and unpaid, and thus triggers the running of interest on that deficiency, when the overpayment balance, after the application to the succeeding tax year's estimated taxes, is less than the deficiency for the overpayment year.

Pursuant to Revenue Ruling 84-58, 1984-1 C.B. 254, which modified Revenue Ruling 77-475, the Service generally was crediting a reported overpayment of tax against the taxpayer's first installment of estimated income tax for the succeeding tax year unless the taxpayer attached a statement to its return that designated otherwise. However, in *May Department Stores Co. v. United States*, 36 Fed. Cl. 680 (1996), the Court of Federal Claims concluded that the assumption behind the default rule in Revenue Ruling 84-58 was that the taxpayer had underpaid its first installment of estimated tax for the succeeding tax year. Thus, a return overpayment will not be deemed to be credited for interest purposes to an installment of estimated tax due prior to the filing of the prior year's return if the taxpayer did not designate the particular installment of estimated tax against which to apply the return overpayment and the installments of estimated tax due prior to the filing of the prior year's return were fully paid without the application of the return overpayment. *May Department Stores Co. v. United States*, 36 Fed. Cl. 680 (1996). On August 4, 1997, the Service acquiesced in the *May Department Stores* decision. *May Department Stores Co. v. United States*, AOD CC-1997-008.[4]

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[4] The *May Department Stores* action on decision provides that,

> for deficiency interest purposes, where a taxpayer does not initially designate a reported overpayment to satisfy a particular installment [of estimated tax] for the following year, and crediting of the return overpayment is not necessary to fully pay an installment of estimated tax due prior to the filing of

In light of the *May Department Stores* decision, the Service has reconsidered the manner in which interest on a subsequently determined deficiency is computed under I.R.C. § 6601(a) when the taxpayer makes an election to apply an overpayment to the succeeding year's estimated taxes. When a taxpayer elects to apply an overpayment to the succeeding year's estimated taxes, the overpayment is applied to unpaid installments of estimated tax due on or after the date(s) the overpayment arose, in the order in which they are required to be paid to avoid an addition to tax for failure to pay estimated tax under I.R.C. § 6655 with respect to such year.

The date the overpayment becomes a payment on account of the succeeding year's estimated tax determines the date the prior year's tax became unpaid for purposes of I.R.C. § 6601(a). Prior to that date the government has had the use of the funds with respect to the prior year's tax, and no interest is payable on the overpayment that is the subject of the taxpayer's election. See I.R.C. § 6402(b); Treasury Reg. § 301.6402-3(a)(5) and § 301.6611-1(h)(2)(vii). Interest should be charged from the point the prior year's tax is both due and unpaid. *May Department Stores Co. v. United States*, 36 Fed. Cl. 680 (1996), acq. AOD CC-1997-008 (Aug. 4, 1997); *Avon Products, Inc. v. United States*, 588 F.2d 342 (2d Cir. 1978); Rev. Rul. 88-98, 1988-2 C.B. 356. Revenue Ruling 84-58 requires the taxpayer to attach a statement to its return, designating the installment of estimated tax against which the overpayment should be applied. However, we now think that a taxpayer may make a retroactive designation if it made the election to credit the return overpayment on the original return without designating a specific installment and the period of limitations for filing a refund claim has not expired.

[redacted]'s Tax Year [redacted] does not fit within the fact pattern set forth in *May Department Stores* because [redacted] had not fully paid its first installment of estimated tax for Tax Year [redacted] without the application of a portion of the return overpayment for Tax Year [redacted]. [redacted] now wishes to apply a portion of the [redacted] overpayment to the first installment of [redacted] estimated taxes due on July 15, [redacted], in the amount of $[redacted]. After the application to this installment, there is a balance of $[redacted] remaining of the [redacted] overpayment. This [redacted] overpayment balance exceeds the [redacted] deficiency of $[redacted], and, therefore, interest on the deficiency did not begin to run from that date.

> the prior year's return, the reported overpayment will not be deemed to be credited to an installment of estimated tax due prior to the filing of the prior year's return.

May Department Stores Co. v. United States, AOD CC-1997-008 (Aug. 4, 1997).

Another portion of the [redacted] overpayment is to be applied against the second installment of [redacted] estimated taxes due on September 15, [redacted] in the amount of $[redacted]. After the application to this installment, there remains a balance of $[redacted] of the [redacted] overpayment. This [redacted] overpayment balance exceeds the [redacted] deficiency of $[redacted], and, therefore, interest on the deficiency did not begin to run from that date. Another portion of the [redacted] overpayment is to be applied against the third installment of [redacted] estimated taxes due on December 15, [redacted], in the amount of $[redacted]. After the application to this installment, there remains a balance of $[redacted] of the [redacted] overpayment. This [redacted] overpayment balance exceeds the [redacted] deficiency of $[redacted], and, therefore, interest on the deficiency did not begin to run from that date. For the fourth quarter due on March 15, [redacted], [redacted] wishes to apply $[redacted] of the [redacted] overpayment.[5] At the time of that application of the [redacted] overpayment credit, the overpayment credit becomes less than the [redacted] deficiency. (Balance of overpayment credit = $[redacted]; deficiency = $[redacted]). It is at this time that the [redacted] deficiency becomes both due and unpaid and interest begins to run. Thus, under [redacted]'s revised request, interest should not have accrued on any portion of [redacted]'s deficiency in tax for Tax Year [redacted] prior to such date (March 15, [redacted]. H.R. Rep. No. 98-432 (Part I), 98th Cong., 1st Sess. 190 (Oct. 21, 1983); *see also* Rev. Rul. 88-98, 1988-2 C.B. 356.

Additionally, as noted above, since the balance of the overpayment after the application to pay the first, second and third installments still exceeded the deficiency of $[redacted], interest on the deficiency did not begin to run from the due date of those installments. However, once the balance of the overpayment was applied to pay the fourth installment, the deficiency for [redacted] exceeded the overpayment balance and interest should begin to run. At this time the deficiency became both due and unpaid.

[redacted] is seeking a refund of interest past March 15, [redacted] ("prorated" based on how much credit elect overpayment remains available to apply to the deficiency). As noted above, however, since the balance of the overpayment was less than the deficiency, after application to the fourth installment, deficiency interest begins to run on the entire deficiency at that point, i.e., March 15, [redacted]. It is at that time that the deficiency became both due and unpaid. [redacted] is not entitled to a "prorated" accrual of deficiency of interest. Once the overpayment is less than the deficiency, deficiency interest runs on the entire deficiency.

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[5] [redacted]'s fourth quarter estimate is the same: $[redacted]; however, Mitsui made a fourth quarter payment from other funds in the amount of $[redacted] and therefore, only needs $[redacted] of the overpayment ($[redacted] + $[redacted] = $[redacted]).

2. The Statute of Limitations Does Not Bar [redacted]'s Subsequent Claim For Refund.

I.R.C. § 6511 requires that a claim for refund be filed within three years from the time the return was filed or two years from the time the tax was paid. There is no dispute that [redacted]'s original claim for a refund was timely. Now, however, [redacted] requests an additional refund of interest by changing the original facts. [redacted]'s additional request would be barred by the statute of limitations if considered a new claim for a refund.

The Regulations require that a claim for refund "set forth in detail each ground upon which a credit or refund is claimed and facts sufficient to apprise the Commissioner of the exact basis thereof." Treas. Reg. § 301.6402-2(b). The taxpayer must "reasonably and substantially" comply with the statute. *Scovill Mfg. Co. v. Fitzpatrick*, 215 F.2d 567, 570 (2d Cir. 1954). The taxpayer may not raise any claim not previously addressed in a claim for refund. *United States v. Felt & Tarrant Mfg. Co.*, 283 U.S. 269 (1931).

"...[W]here a timely general claim is filed, and a subsequent specific claim follows, before rejection[6], for a refund of the same taxes, the latter is an amendment to the former, and the two become "but a claim, single and indivisible, the new indissolubly welded into the structure of the old," especially where, as here, ... the identity of the amounts sought to be recovered is clear. *United States v. Memphis Cotton Oil Co.*, 288 U.S. 62 (1933). In *Memphis*, the original claim lacked definiteness and the taxpayer was allowed to amend it. In contrast, in *United States v. Henry Prentiss & Co.*, 288 U.S. 73 (1933), the amendment was so far reaching as to destroy the identity of the original claim or cause of action, and was not permissible after the statute of limitations had expired. Thus, "[w]here the amendment is inconsistent with the former claim, or has injected new and unrelated matter, we have not allowed it, but where it is germane to the original claim and sets up matter discovered in the course of the investigation of the original one, we have allowed it." *Consolidated Coppermines Corp. v. United States*, 296 F. 2d 743, 745 (Ct. Cl. 1962). *See also, Addressograph-Multigraph Corp. v. United States*, 78 F. Supp. 111 (Ct. Cl. 1948). In *Addressograph*, the taxpayer made no claim in

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[6] No amendment of a claim is allowed after final Service action. An amendment is too late after the Service has disallowed the claim. *United States v. Memphis Cotton Oil Co.*, 288 U.S. 62 (1933). The First and Second Circuits have held that the same rule applies when the Service has allowed a claim. *Edwards v. Malley*, 109 F.2d 640 (1st Cir. 1940); *New York Trust Co. v. United States*, 87 F.2d 889 (2d Cir. 1937), *cert. denied*, 301 U.S. 704 (1937).

its original request for refund of a right to amortization of engineering expense, although it did claim depreciation on other items, but in the course of the investigation by the revenue agent it was concluded that the taxpayer was entitled to such deduction. The Court concluded that "the amendment merely made more definite the matters already within the knowledge of the Commissioner..." *Addressograph* 78 F. Supp. at 122.

"A taxpayer might obtain a recovery in his refund suit on a ground other than that specified in his claim if he can establish adequate notification to the Internal Revenue Service of an intention to claim a refund on that ground." *Union Pacific Railroad Co. v. United States*, 389 F.2d 437 (1968). The test is whether the facts upon which the amended claim is based are such as would necessarily have been disclosed by the investigation of the original claim so that no additional investigation of the facts is necessary in order to pass upon the merits of the amended claim. *Pink v. United States*, 105 F.2d 183 (2d Cir. 1939). *See e.g., Standard Lime and Cement Co. v. United States*, 165 Ct. Cl 180, 329 F.2d 939 (1964) (Commissioner had been given timely notice of the ground for relief when percentage depletion allowance computation as a ground for refund was amended to use a different method). "[E]ach case must be decided on its own peculiar set of facts with a view towards determining whether under those facts the Commissioner knew, or should have known, that a claim was being made." *Newton v. United States*, 163 F. Supp. 614, 619 (Ct. Cl. 1958).

[redacted] is seeking a larger refund based on its revised set of facts. Arguably, these facts were within the knowledge of the Commissioner. [redacted]'s refund claim is based on the same grounds, the use of money principles; the only change is how much [redacted] should have made in each installment of estimated tax. In all other respects, the facts are the same as in the original claim. The taxpayer is merely offering an alternative characterization of those facts. *United States v. Andrews*, 302 U.S. 517 (1938). Thus, [redacted]'s second claim does not really require examination of new matters that would not have been disclosed by an investigation of the original claim. *See also*, Priv. Ltr. Rul. 96-49-005 (August 22, 1996). Therefore, case law would consider [redacted]'s second claim an amendment to the first claim and consequently timely.

3. <u>The taxpayer may retroactively amend its Form 2220 to change the amounts of its estimated payments.</u>

[redacted] has revised its Form 2220 in its most recent request to acquire a larger refund of interest. [redacted], in effect, is manipulating numbers, retroactively, to obtain a tax advantage: less deficiency interest. Form 2220 is not binding on the Service, however. It is a taxpayer generated document relying solely on estimates; the taxpayer estimates how much tax it will be required to pay in a subsequent year and estimates how much

its quarterly payments should be to meet that tax obligation. [redacted] now simply wishes to reestimate its quarterly payments. It is the position of the IRS National Office that as a policy matter, we will allow taxpayers such as [redacted] to retroactively revise their Forms 2220. Please note, however, that these revised Forms 2220 must comply with the requirements of section 6655 and the regulations thereunder. We recommend that you verify that the taxpayer's revisions are reasonable under section 6655.

CONCLUSION:

Based on the foregoing, we recommend that you allow the refund of interest requested by the taxpayer for the period July 15, [redacted] through March 15, [redacted]. We do not recommend a refund of interest for any subsequent period as requested by the taxpayer. As noted previously, we also recommend that you verify that [redacted]'s revised Form 2220 complies with section 6655. Should you have any questions regarding this matter, please contact Jeannette D. Pappas of our office at (212) 264-1595, Ext. 243.

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